TURKEY

OCTOBER 2023

COUNTRY REPORT

TURKEY
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KEY TAKEAWAYS

MOST LIKELY REGIMES & THEIR PROBABILITIES	
18-MONTH	AKP Coalition 80%
FIVE-YEAR	AKP Coalition 70%

FORECASTS OF RISK TO INTERNATIONAL BUSINESS				
	TURMOIL	**FINANCIAL TRANSFER**	**DIRECT INVESTMENT**	**EXPORT MARKET**
18-MONTH	High	C+	B	B-
FIVE-YEAR	Moderate	C+	B	B-

( ) Indicates change in rating
* Indicates forecast of a new regime

KEY ECONOMIC FORECASTS			
	REAL GDP GROWTH (%)	**INFLATION (%)**	**CURRENT ACCOUNT ($bn)**
2018-2022(AVG)	4.5	27.1	-19.47
2023(F)	3.8	52.7	-55.40
2024-2028(F)	3.2	19.6	-33.20

CONTINUED POLICY UNCERTAINTY

The People’s Alliance, a four-party coalition dominated by President Recep Tayyip Erdoğan’s AKP, retained 323 seats in the 600-member GNA at parliamentary elections held on May 14, and the president secured another five-year term by taking 52.2% of the vote in a run-off election held two weeks later. The key question coming out of the elections was whether the victory would be followed by the adoption of a more western-focused foreign policy and the embrace of a more orthodox approach to economic affairs or would be interpreted by the president as a mandate to persist with policies that have alienated Turkey’s NATO partners and sent investors scurrying for the exits.

More than five months later, the answer is not entirely clear. In July, Erdoğan dropped his objections to Sweden’s bid for NATO membership and he has also sought a rapprochement with Greece, with which Ankara cut ties last year to protest Athens’ interference in Turkey’s efforts to purchase F-16 fighters from the US. However, the gestures are purely transactional and the president could reverse course abruptly if his diplomatic objectives are thwarted.

The conflict between Israel and Hamas has complicated relations between Turkey and the US, which earlier this month castigated Turkey for impeding the ongoing battle against Islamic State extremists in northern Syria, to the detriment of regional stability and security. Against that backdrop, and with some

US lawmakers attempting to link the sale of the F-16s to Turkey's adoption of a pro-Israel posture on the Gaza crisis, there is still cause to question when or if the GNA will ratify Sweden's NATO accession.

Similarly, while Erdoğan has made known his desire to resume accession talks with the EU, his threat to pull Turkey out of the Council of Europe to protest an order from the European Court of Human Rights to review the convictions of thousands of alleged participants in a failed 2016 coup will hardly improve Turkey's already slim chances of building support for its bid.

The dismissive response to the ECHR is in part designed to stoke nationalist sentiment with the aim of boosting the government's public support ahead of next year's municipal elections. That same consideration likely explains Erdoğan's recent shift away from unorthodox economic policies that at the very least hindered the ability of policy makers to stabilize the currency and rein in inflation, resulting in economic hardships that contributed to the AKP's poor showing in urban centers at the elections in May.

The hope is that the policy moves will help to bolster the lira and ease pressure on the supply of dollars. However, investors remain wary, and many intend to steer clear of the lira as long as real interest rates remain deeply in negative territory. Central Bank Gov. Hafize Gaye Erkan has pleaded patience as policy makers proceed gradually with the aim of minimizing the shocks generated by the corrective measures.

But it is uncertainty, not impatience, that is keeping investors on the sidelines. If Erkan is permitted to continue implementing the revised strategy, capital inflows will eventually resume. But given Erdoğan's oft-stated preference for low interest rates, the maintenance of which was a central plank of his campaign platform, there is justifiable concern that he might pull the plug on normalization if the economic results do not bring an improvement in the AKP's standing among the electorate. The risk of another U-turn will only increase with the approach of municipal elections in March 2024.

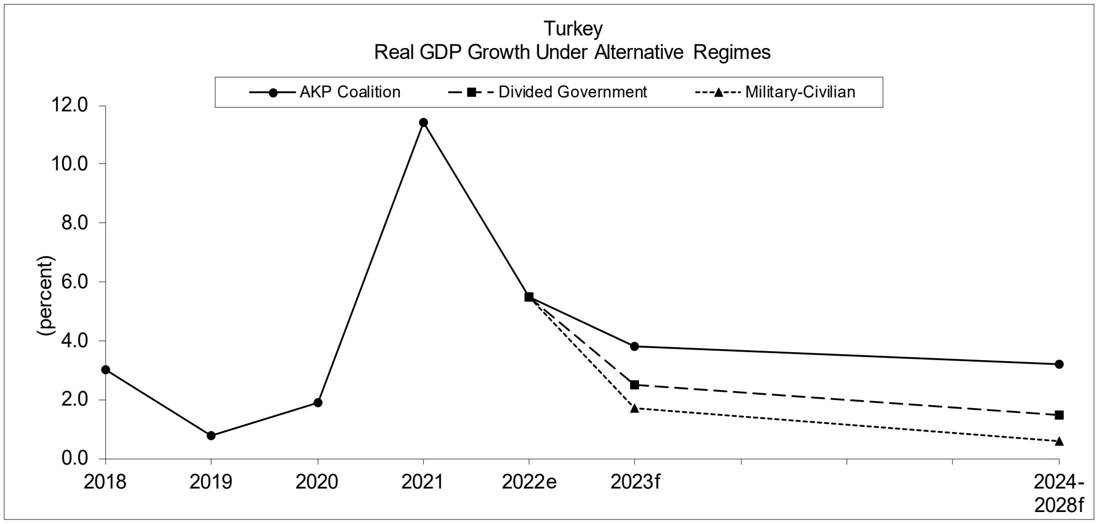
Year-on-year real economic expansion averaged close to 4% in the first half of 2023, but the shift in policy focus from promoting growth to taming inflation points to a deceleration in the second half. Assuming no departures from the current policy course, real GDP growth will slow to 3% in 2024, as investment in reconstruction in areas affected by a devastating earthquake earlier this year puts a floor under the slowdown. However, the risk of unpredictable policy shifts that trigger damaging instability cannot be ruled out.

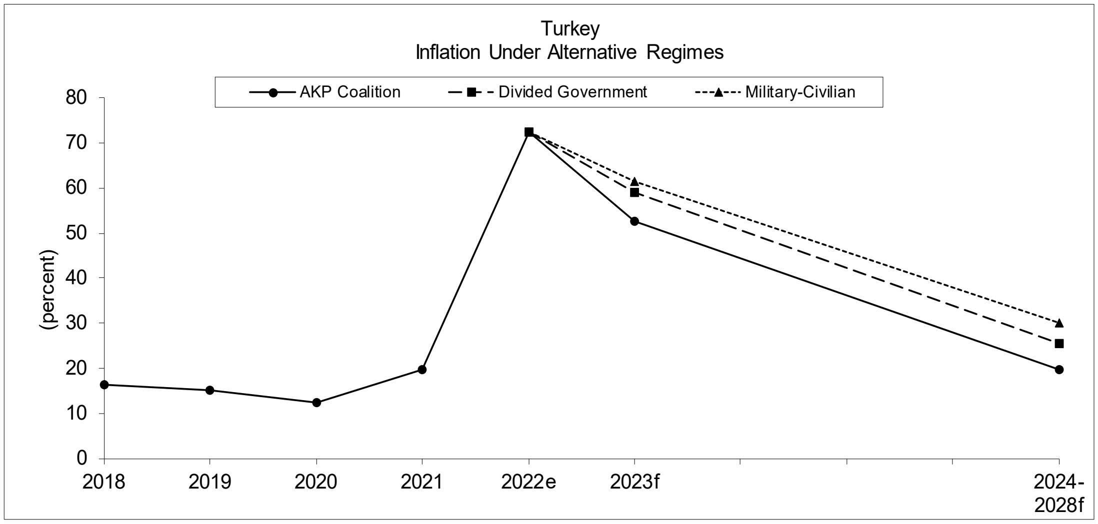
ECONOMIC FORECASTS FOR THE THREE ALTERNATIVE REGIMES									
	AKP Coalition			Divided Government			Military-Civilian		
	GROWTH (%)	INFLATION (%)	CACC ($bn)	GROWTH (%)	INFLATION (%)	CACC ($bn)	GROWTH (%)	INFLATION (%)	CACC ($bn)
2023	3.8	52.7	-55.40	2.5	59.1	-67.80	1.7	61.3	-69.20
2024-2028	3.2	19.6	-33.20	1.5	25.6	-44.70	0.6	30.1	-23.30

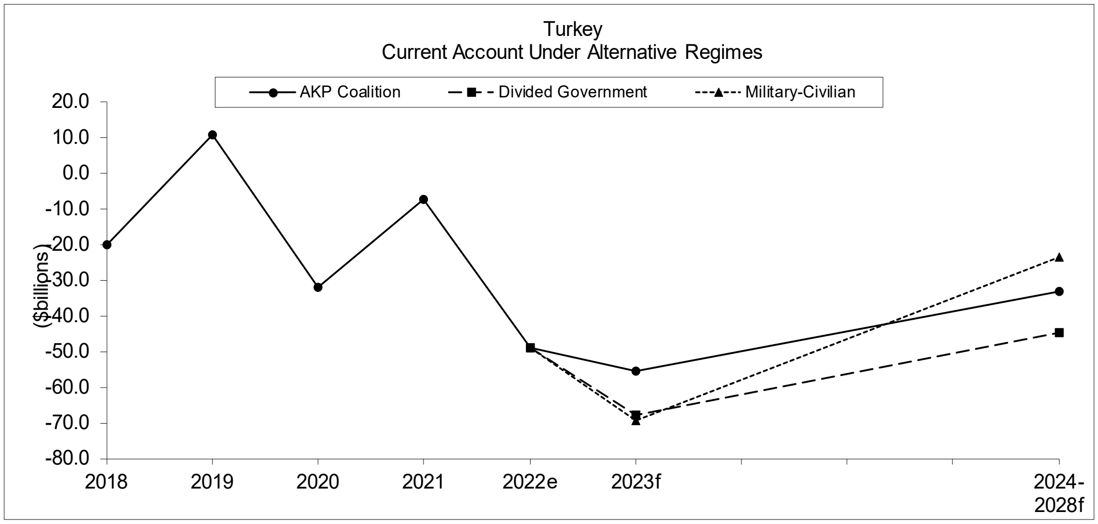
REGIME, BUSINESS & INVESTMENT FORECASTS

SUMMARY OF 18-MONTH FORECAST				
REGIMES & PROBABILITIES		AKP Coalition 80%	Divided Government 15%	Military-Civilian 5%
RISK FACTORS	**CURRENT**			
Turmoil	High	Same	SLIGHTLY MORE	MORE
Investment				
Equity	Moderate	SLIGHTLY LESS	Same	Same
Operations	Moderate	Same	SLIGHTLY MORE	SLIGHTLY MORE
Taxation	Moderate	Same	Same	MORE
Repatriation	Low	SLIGHTLY MORE	MORE	MORE
Exchange	Moderate	SLIGHTLY MORE	MORE	MORE
Trade				
Tariffs	Moderate	SLIGHTLY LESS	Same	Same
Other Barriers	Moderate	Same	Same	SLIGHTLY MORE
Payment Delays	Moderate	Same	SLIGHTLY MORE	MORE
Economic Policy				
Expansion	Moderate	SLIGHTLY MORE	MORE	MORE
Labor Costs	Low	SLIGHTLY MORE	Same	Same
Foreign Debt	High	Same	Same	SLIGHTLY MORE
SUMMARY OF FIVE-YEAR FORECAST				
REGIMES & PROBABILITIES		AKP Coalition 70%	Divided Government 20%	Military-Civilian 10%
RISK FACTORS	**BASE**			
Turmoil	Moderate	Same	SLIGHTLY MORE	SLIGHTLY MORE
Restrictions				
Investment	Moderate	SLIGHTLY LESS	Same	SLIGHTLY MORE
Trade	Moderate	SLIGHTLY LESS	Same	Same
Economic Problems				
Domestic	Moderate	SLIGHTLY MORE	MORE	MUCH MORE
International	High	Same	SLIGHTLY MORE	SLIGHTLY MORE

* When present, indicates forecast of a new regime


Turkey
Real GDP Growth Under Alternative Regimes
AKP Coalition
Divided Government
Military-Civilian
(percent)
12.0
10.0
8.0
6.0
4.0
2.0
0.0
2018
2019
2020
2021
2022e
2023f
2024-2028f


Turkey
Inflation Under Alternative Regimes
AKP Coalition
Divided Government
Military-Civilian
(percent)
80
70
60
50
40
30
20
10
0
2018
2019
2020
2021
2022e
2023f
2024-2028f


Turkey
Current Account Under Alternative Regimes
AKP Coalition
Divided Government
Military-Civilian
($billions)
20.0
10.0
0.0
-10.0
-20.0
-30.0
-40.0
-50.0
-60.0
-70.0
-80.0
2018
2019
2020
2021
2022e
2023f
2024-2028f

Turkey
Econometric Data

	2013-2017 Average	2018-2022 Average	2013	2014	2015	2016	2017
Domestic Economic Indicators							
GDP (Nominal, $bn)	897.12	794.89	956.68	938.74	862.41	868.28	859.49
Per Capita GDP ($)	11493	9490	12623	12163	11025	10952	10702
Real GDP Growth Rate (%)	6.1	4.5	8.5	4.9	6.1	3.3	7.5
Inflation Rate (%)	8.6	27.1	7.5	8.9	7.7	7.8	11.1
Capital Investment ($bn)	261.05	223.26	271.18	269.85	254.88	252.74	256.62
Capital Investment/GDP (%)	29.2	28.0	28.4	28.8	29.6	29.1	29.9
Budget Revenues ($bn)	186.43	156.74	204.45	194.46	177.10	183.19	172.93
Budget Revenues/GDP (%)	20.8	19.8	21.4	20.7	20.5	21.1	20.1
Budget Expenditures ($bn)	196.80	175.34	214.18	205.00	185.73	193.08	186.03
Budget Expenditures/GDP (%)	21.9	22.2	22.4	21.8	21.5	22.2	21.6
Budget Balance ($bn)	-10.38	-18.60	-9.73	-10.54	-8.63	-9.89	-13.10
Budget Balance/GDP (%)	-1.1	-2.4	-1.0	-1.1	-1.0	-1.1	-1.5
Money Supply (M1, $bn)	120.57	170.21	120.34	118.16	114.37	126.56	123.42
Change in Real Wages (%)	9.6	-9.6	11.8	13.0	15.2	11.1	-3.2
Unemployment Rate (%)	10.2	12.0	8.9	9.9	10.3	10.9	10.9
International Economic Indicators							
Foreign Direct Investment ($bn)	14.24	11.28	13.56	13.34	19.26	13.83	11.19
Forex Reserves ($bn)	97.41	71.43	110.96	106.91	92.93	92.06	84.19
Gross Reserves (ex gold, $bn)	97.41	71.43	110.96	106.91	92.93	92.06	84.19
Gold Reserves ($bn)	19.14	35.02	20.08	20.40	17.61	14.05	23.54
Gross reserves (inc gold, $bn)	116.55	106.45	131.04	127.31	110.54	106.11	107.73
Total Foreign Debt ($bn)	416.37	433.79	405.16	416.83	402.91	406.13	450.83
Total Foreign Debt/GDP (%)	46.6	54.8	42.4	44.4	46.7	46.8	52.5
Debt Service ($bn)	11.33	20.57	10.79	11.95	10.25	10.96	12.70
Debt Service/XGS (%)	5.0	7.6	4.8	4.9	4.7	5.3	5.5
Current Account ($bn)	-37.19	-19.47	-55.09	-38.02	-26.23	-26.67	-39.96
Current Account/GDP (%)	-4.1	-2.4	-5.8	-4.1	-3.0	-3.1	-4.6
Current Account/XGS (%)	-16.5	-7.1	-24.5	-15.6	-12.0	-12.9	-17.3
Exports ($bn)	163.48	201.51	167.40	173.29	154.87	152.65	169.21
Imports ($bn)	222.68	244.35	249.28	239.87	203.87	192.57	227.79
Trade Balance ($bn)	-59.19	-42.84	-81.88	-66.58	-49.00	-39.92	-58.58
Exports of Services ($bn)	53.92	63.03	49.63	63.12	56.19	46.70	53.97
Income, credit ($bn)	5.01	6.76	5.29	4.91	4.51	5.36	4.96
Transfers, credit ($bn)	2.48	0.71	2.38	2.63	2.47	2.17	2.75
Exports G&S ($bn)	224.89	272.02	224.70	243.95	218.04	206.88	230.89
Liabilities ($bn)	4.39	10.37	8.28	4.75	3.42	3.14	2.36
Net Reserves ($bn)	112.16	96.08	122.76	122.56	107.12	102.97	105.37
Liquidity (months import cover)	6.1	4.9	5.9	6.1	6.3	6.4	5.6
Currency Exchange Rate	2.698	8.603	1.906	2.189	2.726	3.025	3.646
Currency Change (%)	-13.0	-25.2	-5.6	-12.9	-19.7	-9.9	-17.0
Social Indicators							
Population (million)	78.16	83.73	75.79	77.18	78.22	79.28	80.31
Population Growth (%)	1.5	1.2	1.6	1.8	1.3	1.4	1.3
Infant Deaths/1000	20	13	22	21	19	19	18
Persons under Age 15 (%)	25	21	26	26	25	25	25
Urban Population (%)	73	76	72	73	73	73	74
Urban Growth (%)	2.0	2.3	1.6	3.2	1.3	1.4	2.7
Literacy % pop.	95	96	94	95	95	95	96
Agricultural Work Force (%)	24	19	26	26	26	26	18
Industry-Commerce Work Force (%)	26	26	26	26	26	26	27
Services Work Force (%)	49	54	48	48	48	48	55
Unionized Work Force (%)	7	8	6	6	6	8	8
Energy - total consumption (10^{15} Btu)	5.63	6.39	5.09	5.21	5.75	5.97	6.15
Energy - consumption/head (10^{9} Btu)	0.07	0.08	0.07	0.07	0.07	0.08	0.08

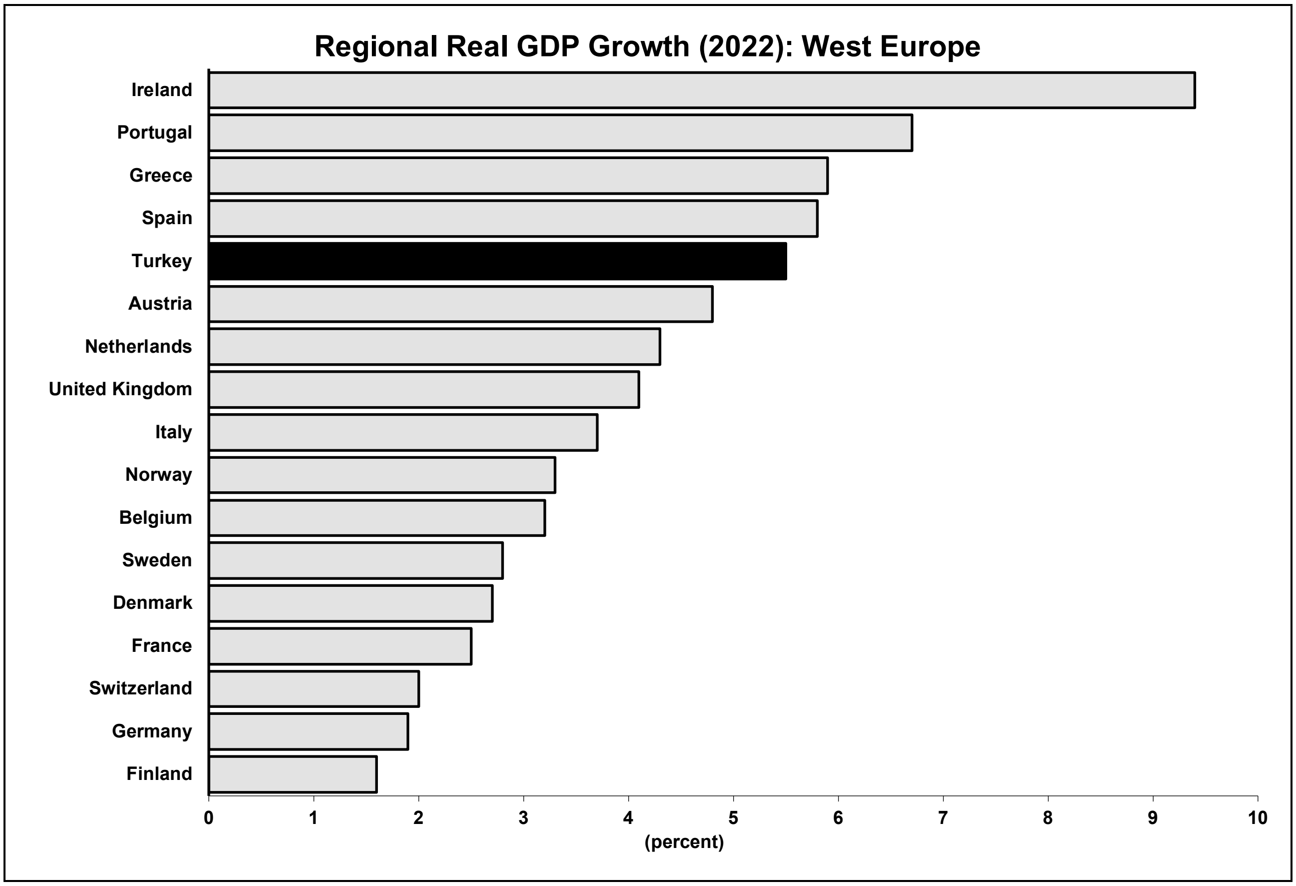
Note: *new liras

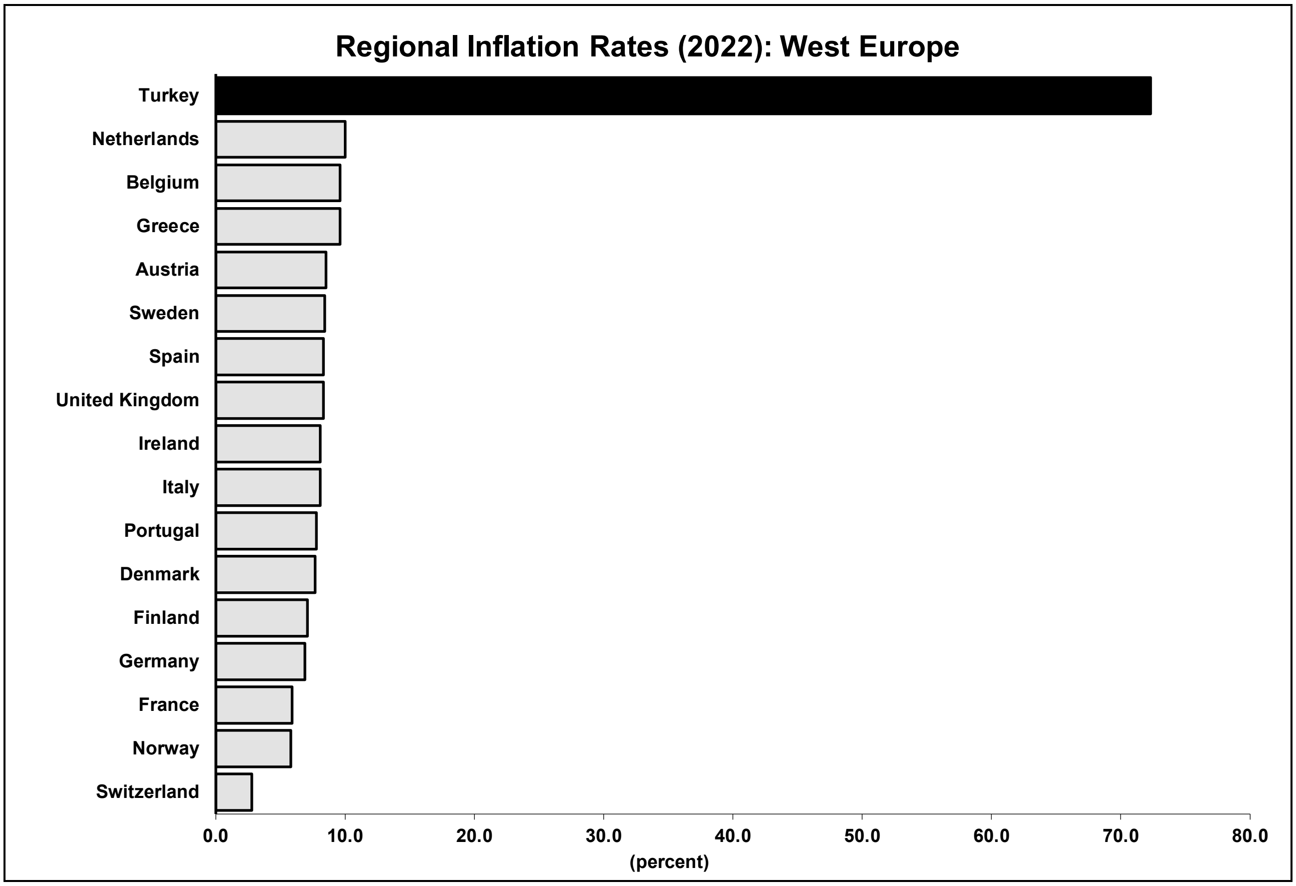
Turkey
Econometric Data

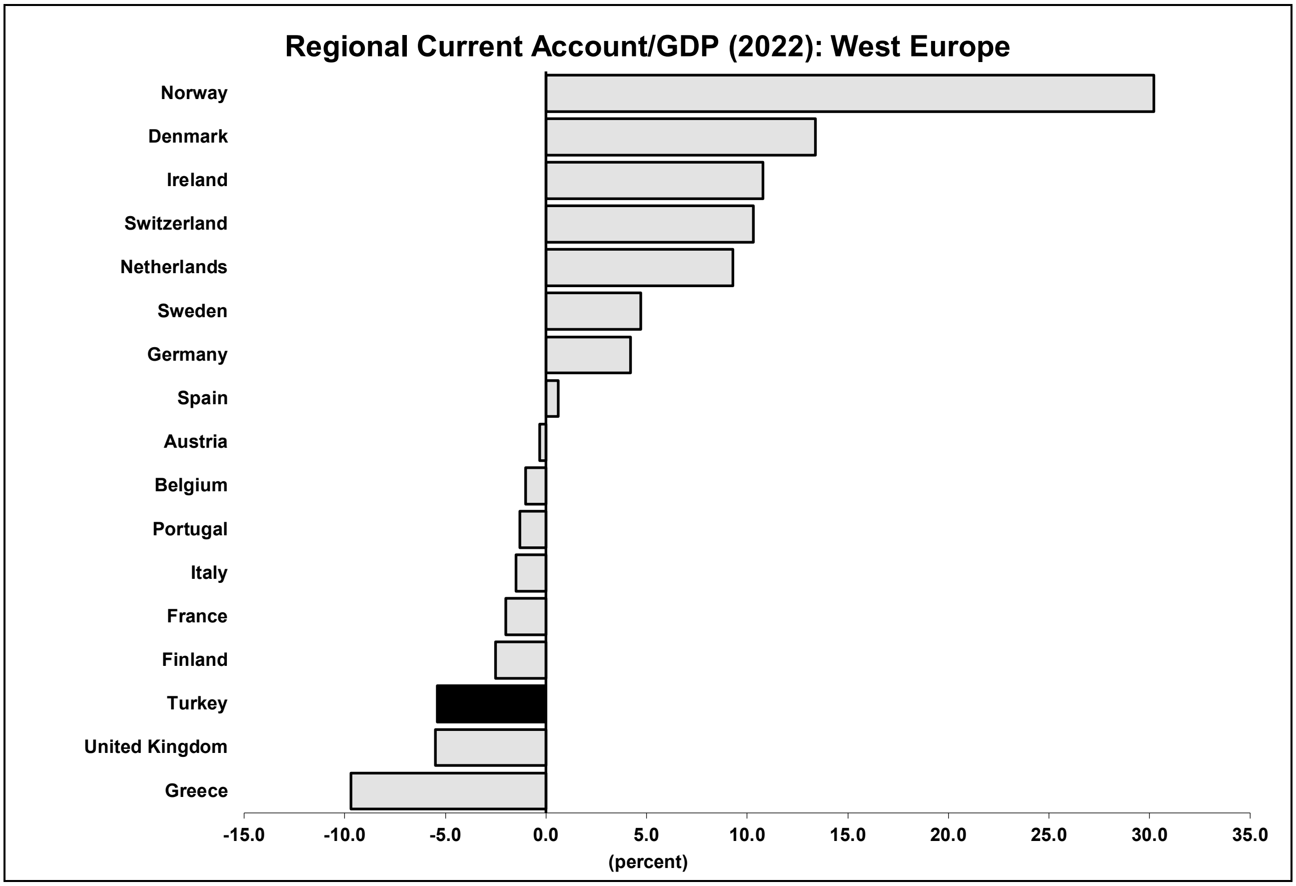
	2013-2017 Average	2018-2022 Average	2018	2019	2020	2021	2022
Domestic Economic Indicators							
GDP (Nominal, $bn)	897.12	794.89	775.64	758.71	719.22	815.20	905.69
Per Capita GDP ($)	11493	9490	9528	9188	8528	9586	10620
Real GDP Growth Rate (%)	6.1	4.5	3.0	0.8	1.9	11.4	5.5
Inflation Rate (%)	8.6	27.1	16.3	15.2	12.3	19.6	72.3
Capital Investment ($bn)	261.05	223.26	230.08	195.56	197.11	229.41	264.13
Capital Investment/GDP (%)	29.2	28.0	29.7	25.8	27.4	28.1	29.2
Budget Revenues ($bn)	186.43	156.74	156.42	154.02	146.52	157.67	169.07
Budget Revenues/GDP (%)	20.8	19.8	20.2	20.3	20.4	19.3	18.7
Budget Expenditures ($bn)	196.80	175.34	171.44	175.97	171.50	180.34	177.46
Budget Expenditures/GDP (%)	21.9	22.2	22.1	23.2	23.9	22.1	19.6
Budget Balance ($bn)	-10.38	-18.60	-15.02	-21.95	-24.98	-22.67	-8.39
Budget Balance/GDP (%)	-1.1	-2.4	-1.9	-2.9	-3.5	-2.8	-0.9
Money Supply (M1, $bn)	120.57	170.21	122.85	125.47	176.30	237.51	188.90
Change in Real Wages (%)	9.6	-9.6	4.3	0.2	-1.9	1.1	-51.8
Unemployment Rate (%)	10.2	12.0	10.9	13.7	13.1	12.0	10.5
International Economic Indicators							
Foreign Direct Investment ($bn)	14.24	11.28	12.45	9.55	7.70	13.33	13.37
Forex Reserves ($bn)	97.41	71.43	72.90	78.61	50.04	72.69	82.89
Gross Reserves (ex gold, $bn)	97.41	71.43	72.90	78.61	50.04	72.69	82.89
Gold Reserves ($bn)	19.14	35.02	20.13	27.09	43.55	38.49	45.85
Gross reserves (inc gold, $bn)	116.55	106.45	93.03	105.70	93.59	111.18	128.74
Total Foreign Debt ($bn)	416.37	433.79	426.33	414.63	430.20	439.26	458.53
Total Foreign Debt/GDP (%)	46.6	54.8	55.0	54.6	59.8	53.9	50.6
Debt Service ($bn)	11.33	20.57	13.73	13.09	21.73	29.39	24.93
Debt Service/XGS (%)	5.0	7.6	5.6	5.1	10.2	10.0	7.1
Current Account ($bn)	-37.19	-19.47	-20.15	10.80	-31.89	-7.23	-48.89
Current Account/GDP (%)	-4.1	-2.4	-2.6	1.4	-4.4	-0.9	-5.4
Current Account/XGS (%)	-16.5	-7.1	-8.2	4.2	-15.0	-2.5	-13.9
Exports ($bn)	163.48	201.51	178.91	182.20	168.38	224.69	253.35
Imports ($bn)	222.68	244.35	219.65	198.98	206.52	254.00	342.59
Trade Balance ($bn)	-59.19	-42.84	-40.74	-16.78	-38.14	-29.31	-89.24
Exports of Services ($bn)	53.92	63.03	59.34	67.22	38.24	61.41	88.95
Income, credit ($bn)	5.01	6.76	6.13	6.33	6.22	6.72	8.42
Transfers, credit ($bn)	2.48	0.71	0.86	0.97	0.23	1.07	0.44
Exports G&S ($bn)	224.89	272.02	245.24	256.72	213.07	293.89	351.16
Liabilities ($bn)	4.39	10.37	4.33	4.03	5.73	19.03	18.71
Net Reserves ($bn)	112.16	96.08	88.70	101.67	87.86	92.15	110.03
Liquidity (months import cover)	6.1	4.9	4.8	6.1	5.1	4.4	3.9
Currency Exchange Rate	2.698	8.603	4.846	5.683	7.019	8.892	16.575
Currency Change (%)	-13.0	-25.2	-24.8	-14.7	-19.0	-21.1	-46.4
Social Indicators							
Population (million)	78.16	83.73	81.41	82.58	84.34	85.04	85.28
Population Growth (%)	1.5	1.2	1.4	1.4	2.1	0.8	0.3
Infant Deaths/1000	20	13	17	16	16	8	8
Persons under Age 15 (%)	25	21	24	24	24	16	16
Urban Population (%)	73	76	75	76	75	76	78
Urban Growth (%)	2.0	2.3	2.7	2.8	2.7	0.9	2.3
Literacy % pop.	95	96	96	96	96	96	96
Agricultural Work Force (%)	24	19	19	19	19	19	19
Industry-Commerce Work Force (%)	26	26	27	26	26	26	26
Services Work Force (%)	49	54	54	53	52	56	56
Unionized Work Force (%)	7	8	8	8	8	8	8
Energy - total consumption (10^{15} Btu)	5.63	6.39	6.17	6.20	6.21	6.46	6.89
Energy - consumption/head (10^{9} Btu)	0.07	0.08	0.08	0.07	0.07	0.08	0.08

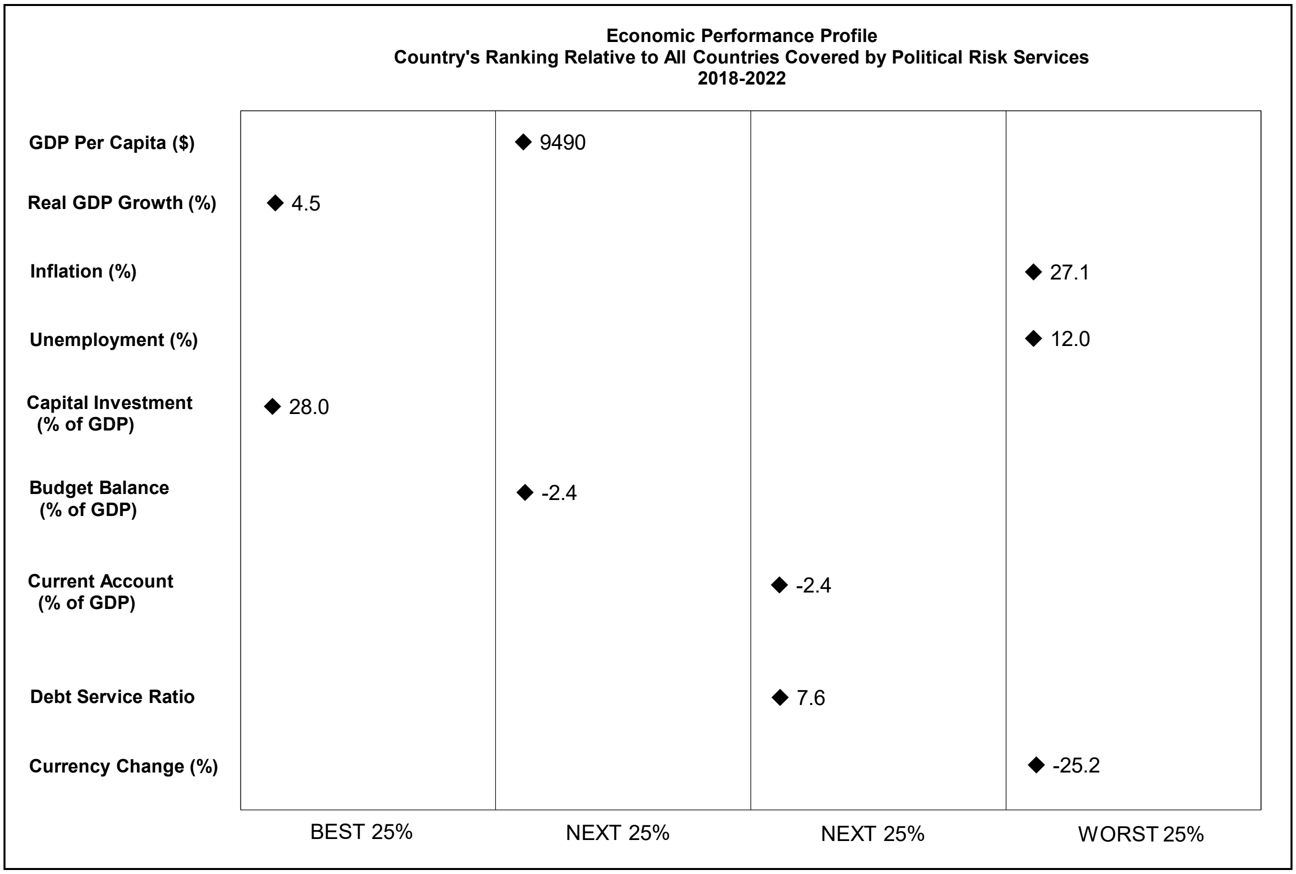
Note: *new liras

INTRA-REGIONAL COMPARISONS






Regional Current Account/GDP (2022): West Europe
Norway
Denmark
Ireland
Switzerland
Netherlands
Sweden
Germany
Spain
Austria
Belgium
Portugal
Italy
France
Finland
Turkey
United Kingdom
Greece
-15.0
-10.0
-5.0
0.0
5.0
10.0
15.0
20.0
25.0
30.0
35.0
(percent)


Economic Performance Profile
Country's Ranking Relative to All Countries Covered by Political Risk Services
2018-2022
GDP Per Capita ($)
9490
Real GDP Growth (%)
4.5
Inflation (%)
27.1
Unemployment (%)
12.0
Capital Investment (% of GDP)
28.0
Budget Balance (% of GDP)
-2.4
Current Account (% of GDP)
-2.4
Debt Service Ratio
7.6
Currency Change (%)
-25.2
BEST 25%
NEXT 25%
NEXT 25%
WORST 25%

GEOPOLITICAL & ECONOMIC ANALYSIS

ERDOĞAN CONTINUES TO CHART HIS OWN DIPLOMATIC COURSE

President Recep Tayyip Erdoğan's consolidation of power over the past two decades has been accompanied by an increasing reliance on military intervention as an instrument of Turkish diplomacy and a stepped-up battle against Kurdish separatists at home and abroad (most notably, in Syria) that has placed it in conflict with the US and other NATO allies even as Ankara has pursued closer relations with Russia. In addition to the adoption of a more assertive and less westward-facing foreign policy posture, the government has also chartered a new course for economic policy, embracing a heterodox monetary strategy that has shaken investor confidence and contributed to chronic market instability, with negative consequences for living standards.

Despite those liabilities, the People's Alliance, a four-party coalition dominated by Erdoğan's Justice and Development Party (AKP), retained 323 seats in the 600-member Grand National Assembly (GNA) at parliamentary elections held on May 14, and the president secured another five-year term by taking 52.2% of the vote in a run-off election held two weeks later. The key question coming out of the elections was whether Erdoğan would interpret his victory as a disaster narrowly averted—prompting a westward pivot on the diplomatic front and the embrace of a more orthodox approach to economic affairs—or a mandate to persist with policies that have alienated Turkey's NATO partners and sent investors scurrying for the exits.

More than five months later, the answer is not entirely clear. In July, Erdoğan dropped his objections to Sweden's bid for NATO membership, which he had blocked over the latter's alleged harboring of individuals that Ankara has designated as terrorists. As promised, the government submitted legislation approving Sweden's accession to the GNA for ratification in late October.

Erdoğan has also sought a rapprochement with Greece, with which he cut ties last year to protest Athens' interference in Turkey's efforts to purchase F-16 fighters from the US. He met with Prime Minister Kyriakos Mitsotakis on the sidelines of a NATO Summit in Vilnius, Lithuania in July, their first encounter since March 2022, and the two leaders met again for more substantive talks while in New York for UN General Assembly in September. Erdoğan and Mitsotakis agreed to restart meetings of the High-Level Cooperation Council (HLCC), which was established in 2010 as a mechanism for managing bilateral disputes but has not convened since 2016.

As with approval of Sweden's NATO membership, the signs of a thaw with Greece are welcome, but the gestures are transactional, and do not appear to reflect a broader shift in strategy by Erdoğan. The overtures to Athens are designed to overcome an obstacle to enhancing Turkey's military capacity, and there were some signals from Ankara that Erdoğan might slow-walk approval of Sweden's entry into

NATO but took action after the recent outbreak of war in the Middle East added to the urgency surrounding the purchase of the F-16s.

There are still questions surrounding the military sale, as the conflict between Israel and Hamas has complicated relations between Turkey and the US. In contrast to US President Joe Biden, who has declared his unreserved support for Israel, Erdoğan has expressed sympathy for the aims (if not the methods) of Hamas and complained that the deployment of a US naval vessel to the Mediterranean is undermining his government's efforts to mediate a resolution to the crisis in Gaza.

Washington and Ankara have conflicting goals elsewhere in the Middle East and have long been at odds over armed Kurdish militias in northeastern Syria that the US view as allies and Turkey considers to be terrorists. The US provoked outrage in Ankara earlier this month by shooting down a Turkish drone in northern Syria and subsequently issuing a statement castigating Turkey for impeding the ongoing battle against Islamic State extremists, to the detriment of regional stability and security. Against that backdrop, there is still cause to question whether or how quickly the GNA will ratify Sweden's accession to NATO, particularly with some US lawmakers now attempting to link the sale of the F-16s to Turkey's adoption of a pro-Israel posture on the Gaza crisis.

Erdoğan's about-face on NATO expansion (including an expressed openness to Ukraine's eventual entry) was accompanied by calls from Ankara to revive Turkey's dormant bid to join the EU. However, his efforts to mend fences with the NATO/EU partners do not extend as far as severing Ankara's ties with Moscow, a relationship the president clearly sees as increasing his leverage in negotiations with the US and the EU. Nor has Erdoğan given any indication that his ambition to join the EU might provide motivation to keep his authoritarian inclinations in check.

Indeed, he has pushed back aggressively against an order from the European Court of Human Rights (ECHR) to review the convictions of thousands of alleged participants in a failed 2016 coup that were allegedly based almost entirely on the defendants' use of the Bylock messaging app. Some members of the Council of Europe are demanding Turkey's expulsion from the group if it refuses to act on the judgment of the ECHR, while Erdoğan has threatened that Turkey might exit of its own accord if the ECHR insists on dictating how it metes out justice to enemies of the government. In either case, Turkey's exclusion from membership in the Council of Europe would doom its already slim chances of joining the EU.

INVESTORS REMAIN WARY AS CBRT PURSUES POLICY NORMALIZATION

The dismissive response to the ECHR is in part designed to stoke nationalist sentiment with the aim of boosting the government's public support ahead of next year's municipal elections. That same consideration likely explains Erdoğan's recent shift away from unorthodox economic policies that at the very least hindered the ability of policy makers to stabilize the currency and rein in inflation, resulting in economic hardships that contributed to the AKP's poor showing in Ankara and Istanbul at the elections in May.

The president signaled a change of direction shortly after the election by shaking up the economic policy team in early June, naming Mehmet Simsek, a proponent of economic orthodoxy, as minister of treasury and finance (a position he previously held in 2009-2015), and appointing Hafize Gaye Erkan, a former Goldman Sachs banker, as governor of the Central Bank of the Republic of Turkey (CBRT). Confirmation of a shift came later in the month, when monetary authorities approved the first interest rate hike in more than two years, lifting the benchmark one-week repo rate from 8.5% to 15%.

However, the move proved insufficient to reassure investors, as the lira slid by close to 7% against the dollar in the immediate aftermath of the rate hike and the yield on Turkey's 10-year bonds continued to creep upward, reaching 18% in mid-July. Pressure eased over the summer months, as reduced demand for energy and an increase in tourism receipts enabled Turkey to replenish its depleted reserves, helping to stabilize the currency below TRL27.0 to the dollar through mid-September.

Unfortunately, inflation continued to climb, hitting a nine-month high of 61.8% (year-on-year) in September, despite additional monetary tightening that has seen the benchmark rate rise to 35% as of October. The near-term prospects for a reversal of the price trend are dimmed by the renewed slide of the lira, which hit a record low of TRL28.45 against the dollar on October 31.

For now, policy makers remain committed to policy normalization, as was driven home in late October, when the CBRT scrapped a requirement for banks to buy government bonds as a penalty for charging interest rates above specified limits or undershooting targets for the extension of loans to businesses. The forced bond purchases were one of the key steps taken to mitigate the market disruptions created by Erdoğan's insistence on keeping interest rates low even as inflation soared and the lira plunged against the dollar.

The hope is that the policy moves will help to bolster the lira and ease pressure on the supply of dollars. However, investors remain wary, and many intend to steer clear of the lira as long as real interest rates remain deeply in negative territory. Erkan has pleaded patience as the CBRT proceeds gradually with the aim of minimizing the shocks generated by the corrective measures, while signaling that additional rate hikes are coming as policy makers take the steps necessary to anchor inflation expectations and reverse the inflationary trend as soon as possible.

But it is uncertainty, not impatience, that is keeping investors on the sidelines. If Erkan is permitted to continue implementing the revised strategy, capital inflows will eventually resume. But given Erdoğan's oft-stated preference for low interest rates, the maintenance of which was a central plank of his recent campaign platform, there is justifiable concern that he might pull the plug on normalization if the economic results do not bring an improvement in the AKP's standing among the electorate. The risk of another U-turn will only increase with the approach of municipal elections in March 2024.

INFLATION A KEY RISK

High inflation will remain the main policy challenge for Simsek and Erkan in the near term. The steep rise in the consumer price index since June is the result of a combination of lira depreciation, wage and tax increases, a less favorable base effect, and continued strong domestic demand. The annual average is forecast to exceed 50% this year, and any chance of a significant easing of price pressure in 2024 depends on several factors, including the persistence of a commitment to policy normalization—which will affect inflation expectations and currency volatility—and the trajectory of commodity prices.

Year-on-year real economic expansion averaged close to 4% in the first half of 2023, but the shift in policy focus from promoting growth to taming inflation points to a deceleration in the second half. The manufacturing purchasing managers' index (PMI) has remained below the 50.0 level dividing expansion from contraction since July, and the combination of aggressive monetary tightening (the benchmark interest rate is currently at the highest level in two decades) and persistent high inflation will have a dampening effect on both investment and consumption.

Assuming no departures from the current policy course, real GDP growth will slow to 3% in 2024, as investment in reconstruction in areas affected by a devastating earthquake earlier this year puts a floor under the slowdown. However, the risk of unpredictable policy shifts that trigger damaging instability cannot be ruled out.

Goods exports contracted by 1.8% (year-on-year) through the first eight months of 2023, while imports increased by 2.6%, resulting in a wider trade deficit that was only partially offset by strong growth of services exports. The current account shortfall amounted to $43 billion at the end of August, and the full-year deficit is on track to exceed last year's figure of $48.9 billion. The large external finance requirement implies sustained downward pressure on the lira that will create challenges for monetary authorities.

INTERNATIONAL COUNTRY RISK GUIDE (ICRG) RATINGS

PRS' Country Reports and Economic Forecasts (CREF) and the International Country Risk Guide (ICRG) have been independently back-tested for accuracy and relevance for over 40 years.

In a landmark 2014 study published in the International Journal of Business Studies* – using data on political risk clams and a unique textual-based database of risk realizations – both CREF and ICRG forecasts were found to have "predictive power for both political risk insurance claims as well as political risk events measured by news coverage."

It is therefore instructive to present the scores from Table 1 of the ICRG for a complimentary look at the composite risk scores – calculated by using a combination of the overall political, financial, and economic risk metrics – for the 141+ countries covered each month. Please contact custserv@prsgroup.com for more information.

TABLE 1
COUNTRY RISK, RANKED BY COMPOSITE RISK RATING
OCTOBER 2023 VERSUS NOVEMBER 2022

RANK IN 10/23	COUNTRY	COMPOSITE RISK RATING 10/23	COMPOSITE RISK RATING 11/22	10/23 VERSUS 11/22	RANK IN 11/22
	Very Low Risk				
1	Norway	86.0	87.0	-1.0	2
1	Switzerland	86.0	87.3	-1.3	1
3	Luxembourg	85.8	86.0	-0.3	3
4	Denmark	84.8	84.3	0.5	6
5	Taiwan	84.5	84.3	0.3	6
6	Singapore	84.3	85.8	-1.5	4
7	Ireland	83.8	82.3	1.5	8
8	Saudi Arabia	82.5	85.5	-3.0	5
9	Brunei	81.8	79.5	2.3	16
10	Canada	80.8	82.0	-1.3	10
10	Iceland	80.8	80.5	0.3	14
10	Qatar	80.8	78.8	2.0	17

* C Harvey, et al., "Political Risk Spreads," Journal of International Business Studies, (2014), 471-493.

TABLE 1 COUNTRY RISK, RANKED BY COMPOSITE RISK RATING OCTOBER 2023 VERSUS NOVEMBER 2022					
RANK IN 10/23	COUNTRY	COMPOSITE RISK RATING 10/23	COMPOSITE RISK RATING 11/22	10/23 VERSUS 11/22	RANK IN 11/22
13	United Arab Emirates	80.5	82.3	-1.8	8
14	Netherlands	80.3	79.8	0.5	15
15	Kuwait	80.0	80.8	-0.8	13
	Low Risk				
16	Japan	79.8	76.3	3.5	26
16	Sweden	79.8	81.0	-1.3	12
18	Korea, Republic	79.5	77.8	1.8	22
19	Australia	79.3	81.3	-2.0	11
19	Botswana	79.3	77.0	2.3	24
21	Finland	78.8	78.3	0.5	20
21	New Zealand	78.8	76.0	2.8	27
23	Germany	78.5	78.8	-0.3	17
24	Hong Kong	78.0	74.0	4.0	36
25	Trinidad & Tobago	77.0	77.5	-0.5	23
26	Bahamas	76.8	71.0	5.8	55
26	Portugal	76.8	75.5	1.3	31
28	Austria	76.5	78.5	-2.0	19
28	Oman	76.5	78.3	-1.8	20
30	Czech Republic	75.8	75.5	0.3	31
31	Kazakhstan	75.5	76.0	-0.5	27
32	Guyana	75.3	75.8	-0.5	30
33	Uzbekistan	74.8	73	2.3	43
34	Belgium	74.5	74.5	0.0	35
34	Italy	74.5	73.5	1.0	38
36	Malaysia	74.3	73.5	0.8	38
37	Croatia	73.8	73.8	0.0	37
37	Libya	73.8	70.8	3.0	59
37	Malta	73.8	74.8	-1.0	34

TABLE 1 COUNTRY RISK, RANKED BY COMPOSITE RISK RATING OCTOBER 2023 VERSUS NOVEMBER 2022					
RANK IN 10/23	COUNTRY	COMPOSITE RISK RATING 10/23	COMPOSITE RISK RATING 11/22	10/23 VERSUS 11/22	RANK IN 11/22
37	Panama	73.8	73.5	0.3	38
37	Slovenia	73.8	73.0	0.8	41
37	United Kingdom	73.8	76.8	-3.0	25
37	Uruguay	73.8	75.3	-1.5	33
44	Azerbaijan	73.3	72.5	0.8	43
45	Costa Rica	73.0	72.0	1.0	48
46	Latvia	72.8	71.5	1.3	52
47	Jamaica	72.5	72.3	0.3	46
47	Spain	72.5	72.8	-0.3	42
49	Dominican Republic	72.3	72.5	-0.3	43
50	Brazil	71.8	70.0	1.8	65
50	Chile	71.8	71.8	0.0	49
50	France	71.8	72.3	-0.5	46
50	Israel	71.8	76.0	-4.3	27
54	Bulgaria	71.5	70.8	0.8	59
54	Philippines	71.5	70.8	0.8	59
54	Poland	71.5	71.0	0.5	55
54	Vietnam	71.5	70.8	0.8	59
58	Hungary	71.0	71.5	-0.5	52
58	India	71.0	70.3	0.8	63
60	Guatemala	70.8	71.0	-0.3	55
60	Thailand	70.8	65.0	5.8	88
62	United States	70.5	71.8	-1.3	49
63	China, Peoples' Rep.	70.0	69.5	0.5	67
Moderate Risk					
64	Cyprus	69.8	70.0	-0.3	65
64	Gabon	69.8	66.5	3.3	84
64	Lithuania	69.8	70.3	-0.5	63

TABLE 1 COUNTRY RISK, RANKED BY COMPOSITE RISK RATING OCTOBER 2023 VERSUS NOVEMBER 2022					
RANK IN 10/23	COUNTRY	COMPOSITE RISK RATING 10/23	COMPOSITE RISK RATING 11/22	10/23 VERSUS 11/22	RANK IN 11/22
67	Bahrain	69.3	68.8	0.5	71
68	Estonia	69.0	71.5	-2.5	52
68	Indonesia	69.0	68.3	0.8	73
68	Papua New Guinea	69.0	69.3	-0.3	68
71	Greece	68.8	68.0	0.8	76
71	Mexico	68.8	68.3	0.5	73
73	Congo, Republic	68.5	64.3	4.3	94
73	Iraq	68.5	71.0	-2.5	55
73	Peru	68.5	68.0	0.5	76
76	Namibia	68.3	71.8	-3.5	49
76	Slovakia	68.3	68.8	-0.5	71
78	Algeria	67.8	69.3	-1.5	68
79	Romania	67.3	66.8	0.5	82
80	Ecuador	67.0	68.3	-1.3	73
80	Gambia	67.0	65.0	2.0	88
80	Honduras	67.0	66.8	0.3	82
83	Morocco	66.8	64.5	2.3	92
83	Russia	66.8	66.0	0.8	87
85	El Salvador	66.5	63.8	2.8	98
85	Mongolia	66.5	65.0	1.5	88
85	South Africa	66.5	67.3	-0.8	80
88	Tanzania	66.3	65.0	1.3	88
89	Armenia	66.0	60.0	6.0	110
90	Serbia	65.8	67.3	-1.5	80
91	Guinea-Bissau	65.3	64.0	1.3	96
91	Paraguay	65.3	64.3	1.0	94
93	Jordan	65.0	64.5	0.5	92
94	Albania	64.8	67.8	-3.0	79

TABLE 1 COUNTRY RISK, RANKED BY COMPOSITE RISK RATING OCTOBER 2023 VERSUS NOVEMBER 2022					
RANK IN 10/23	COUNTRY	COMPOSITE RISK RATING 10/23	COMPOSITE RISK RATING 11/22	10/23 VERSUS 11/22	RANK IN 11/22
95	Iran	64.3	66.5	-2.3	84
96	Bolivia	64.0	66.5	-2.5	84
96	Cote d'Ivoire	64.0	62.3	1.8	105
98	Colombia	63.8	64.0	-0.3	96
98	Nicaragua	63.8	62.8	1.0	101
100	Bangladesh	63.5	62.5	1.0	103
100	Togo	63.5	63.3	0.3	100
102	Madagascar	63.0	62.5	0.5	3
103	Zambia	62.3	62.8	-0.5	101
104	Ghana	62.0	58.8	3.3	115
105	Cuba	61.8	69.3	-7.5	68
106	Cameroon	61.5	60.3	1.3	108
107	Moldova	61.3	59.0	2.3	114
107	Ukraine	61.3	51.8	9.5	133
109	Angola	60.5	68.0	-7.5	76
110	Mozambique	60.0	54.5	5.5	128
110	Uganda	60.0	59.3	0.8	113
High Risk					
112	Guinea	59.8	57.3	2.5	124
112	Tunisia	59.8	61.3	-1.5	107
114	Belarus	59.3	57.0	2.3	126
114	Senegal	59.3	58.3	1.0	119
114	Suriname	59.3	58.5	0.8	117
117	Burkina Faso	59.0	59.5	-0.5	111
118	Myanmar	58.3	55.8	2.5	127
119	Ethiopia	58.0	58.5	-0.5	117
120	Mali	57.8	58.8	-1.0	115
121	Zimbabwe	57.5	61.5	-4.0	106

TABLE 1 COUNTRY RISK, RANKED BY COMPOSITE RISK RATING OCTOBER 2023 VERSUS NOVEMBER 2022					
RANK IN 10/23	COUNTRY	COMPOSITE RISK RATING 10/23	COMPOSITE RISK RATING 11/22	10/23 VERSUS 11/22	RANK IN 11/22
122	Egypt	57.3	57.8	-0.5	123
123	Congo, Dem. Republic	57.0	60.3	-3.3	108
123	Sierra Leone	57.0	53.5	3.5	131
125	Haiti	56.8	54.3	2.5	129
125	Kenya	56.8	58.3	-1.5	119
127	Argentina	56.3	63.8	-7.5	98
128	Nigeria	56.0	59.5	-3.5	111
129	Yemen, Republic	55.8	48.3	7.5	138
130	Turkey	55.5	54.3	1.3	129
131	Liberia	55.0	58.0	-3.0	121
131	Venezuela	55.0	58.0	-3.0	121
133	Sri Lanka	54.5	48.5	6.0	137
134	Malawi	52.3	51.0	1.3	134
135	Somalia	51.8	52.0	-0.3	132
Very High Risk					
136	Korea, D.P.R.	49.3	51.0	-1.8	134
136	Pakistan	49.3	51.0	-1.8	134
138	Niger	47.8	57.3	-9.5	124
139	Syria	44.5	43.8	0.8	139
140	Sudan	43.5	43.0	0.5	140
141	Lebanon	34.8	41.3	-6.5	141